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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1958.

No. 402

WILLIAM EUGENE MONDAY, JR.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

WILLIAM EUGENE MONDAY, JR., and
FLORENCE S. MONDAY,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI

To the United States Court of Appeals for the Sixth Circuit.

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To the United States Court of Appeals for the Sixth Circuit.

To the Honorable Justices of the Supreme Court of the United States:

The petitioners pray that a writ of certiorari issue to review the judgments of the United States Court of Ap-

peals for the Sixth Circuit entered in the above cases on February 20, 1958,[1] the petition to rehear being overruled April 29, 1958.

OPINIONS BELOW.

The decisions and orders of the Tax Court are reported in 16 T. C. M. 1 (1957) and appear in R. A. 479a through 504a and 520a through 522a. The one page order of the Court of Appeals of February 20, 1958, is reported in 252 F. 2nd 789, and appears in R. R. 1; and the Court of Appeals order denying petition to rehear on April 29, 1958, appears in R. R. 43b.

JURISDICTION.

The jurisdiction of this Court is invoked under 28 U. S. C. 1254 (1).

QUESTIONS PRESENTED.

The Tax Court assessed petitioner with additional income tax as deficiencies for the years 1946, 1947, 1948, and 1949. The deficiency for 1946 was $66,767.94; the year 1947, $153,186.81; the year 1948, $38,466.41; the year 1949, $16,921.18. The years of 1946 and 1947 were against William Eugene Monday, Jr., and the years of 1948 and 1949 were against William Eugene Monday, Jr., and wife, Florence S. Monday. Mr. Monday filed income tax returns for these years and paid the full tax on his income as a Real Estate Investor. The respondent in 1953 filed notice of claim for additional tax asserting that petitioner Wil-

[1] The record as printed for the Court below consists of the petitions, answers, stipulation, proceedings, and testimony, pages 1a through 477a, and will be referred to as "R. A. 1a et seq."; and contains orders, findings of fact and opinion, motions, orders, decisions, and petitions, pages 478a through 526a, and will be referred to as "R. 478a et seq."; and proceedings in the Court below appear last in the records and will be designated as "R. R. 1a and 1b et seq."

liam Eugene Monday, Jr., was a Real Estate Dealer and assessed additional tax. The Court of Appeals affirmed.

The questions presented are:

1. Can a taxpayer, who is an admitted real estate investor, be deprived of long term capital gains under the provisions of Section 117 (j) of the Internal Revenue Code of 1939 where the gains are derived from the sale of residences,

(a) Owned and continuously rented for more than six (6) months by admitted real estate investor;

(b) Whose only investments are in rental real estate;

(c) Who is neither a contractor nor a builder, and who was in no way connected with the building of the residences;

(d) Who is not a licensed real estate dealer or broker, and has never been so licensed;

(e) Who negotiated no sale himself;

(f) Whose activities in connection with the sale consisted only of accepting unsolicited offers to buy, and in signing the deeds of conveyances and receiving the consideration;

(g) Who reluctantly agreed to the unsolicited sales of a small portion of his rental residences at the insistence and demand of National Housing Authority and Federal Housing Authority officials;

(h) Who never verbally or in writing listed a house for sale with any agent or broker;

(i) Who never advised anyone he had a residence for sale and who did no sales advertising;

(j) Whose background and reputation since 1931 is that of an investor in real estate;

(k) Whose intent at the time of purchase was to rent and pay for the residences over the years and whose intention at no time changed, although he had a ready market for the houses, and hundreds of others of the same type which he owned, and who at all times had rented or offered for rent all of said residences;

(l) Who neither agreed to the sale of a house which was rented and occupied nor disturbed any tenant in his right to possession either by eviction or threat of same, or by offering said house for sale either to the tenant or to anyone else;

(m) Whose primary and practically sole source of income was from rentals which far exceeded his gains from the residences in question;

(n) Who used the income derived from said sales for the purchase of other investment real estate, the improvement of then owned rental property and the meeting of his indebtedness theretofore in existence in connection with rental properties purchased;

(o) Who owned, rented and retained all of the newly purchased residences and owned same at the time of trial some six years later;

(p) Who paid to real estate dealers who made the sales the established real estate commission, although had the residences been held by him primarily for sale in an ordinary business he could have sold them in a very short time to customers without the necessity of paying any commission; and

(q) Whose testimony and that of all other witnesses, both his own and the few witnesses for the Government, and the admissions of the Government's attorney, and the findings of the Tax Court fully and without contradiction, sustain the above statements as being true,

2. Was the finding of fact by the Tax Court that the defense housing units sold during the taxable period were primarily held for sale to customers in the ordinary course of a trade or business then being carried on by petitioner clearly erroneous?

STATUTES INVOLVED.

The statutory provision involved is Section 117 (a) (1), (j) (1), (b) of the Internal Revenue Code of 1939 which is printed in Appendix "A" hereto, page 1a.

STATEMENT.

On July 7, 1953, the Commissioner of Internal Revenue sent petitioner notice of deficiencies in which he determined that William Eugene Monday, Jr., owed as deficiency in income tax for the taxable year 1946 in the amount of $67,535.70 and a deficiency for the year 1947 in the amount of $152,881.20 (R. A. 7a, 10a, 11a, 20a, 24a, 28a).

The petitioners, William Eugene Monday, Jr., and Florence S. Monday, received notice of deficiencies from the Commissioner of Internal Revenue on July 7, 1953, in which he determined that William Eugene Monday, Jr., and Florence S. Monday owed as deficiency in income tax for the taxable year 1948 the amount of $38,446.41 and a deficiency for the year 1949 in the amount of $16,921.18 (R. A. 29a, 32a, 33a, 43a, 45a, 50a, 55a).

The deficiencies were based on the determination by the Commissioner that the proceeds from the sales of defense houses and escrow accounts were taxable as ordinary income and not as capital gains.

Thereafter on October 1, 1953, petitioners duly filed appeals from said determination with the Tax Court of

the United States (R. A. 7a-55a). The cases were tried before the Tax Court on May 16, 17 and 18, 1955, in Knoxville, Tennessee. On January 2, 1957, the Tax Court promulgated its findings of fact and opinion (R. 479a-503a) and entered its decision ordering and deciding that the taxpayers owed the deficiencies in income tax for the taxable years 1946, 1947, 1948, and 1949 in the amounts as determined by the Commissioner of Internal Revenue (R. 504a). Thereafter a motion to vacate the decisions entered on January 16, 1957, was filed and that an order be entered under Rule 50 (R. 505a), and such order was entered on February 7, 1957 (R. 519a), and the decision was entered on February 8, 1957 (R. 521a-522a).

Petitions for review were filed in the United States Court of Appeals on May 3, 1957, to review the orders and decisions entered by the Tax Court on February 7 and 8, 1957 (R. 523a-525a).

The United States Court of Appeals affirmed the Tax Court on the ground that the findings were not in any respect clearly erroneous (R. R. 1a).

REASONS FOR GRANTING THE WRIT.

I.

The Decision in the Case at Bar Is in Direct Conflict With the Decision of the Third Circuit in Curtis Company v. Commissioner (March 30, 1956), 232 F. (2nd) 167, on the Question of Erroneous Conclusions and Findings of Fact Induced by Erroneous View of Law.

In the **Curtis** case, the action of the taxpayer was expressly pointed out as to placing him in the position of being able to treat the sale of rental houses as capital gain. These houses were held for rental investment and not real estate selling.

The Tax Court held that the taxpayer was not entitled to the benefit of capital gains provisions of the income tax statute; however, upon appeal the Third Circuit reversed the Tax Court, stating:

> "(2) In the typical case it is clear that the property owner did not intend to engage in the business of buying and selling real estate when he acquired or developed it, but on the contrary intended only to rent it. At the time he may have been restrained from selling by wartime legislation or the terms of a government loan. But years later, his intention changes or the government restrictions are removed, and he proceeds to sell the property. The test as to whether the capital gain provisions apply in such event is, at bottom, whether the purpose of the sales is primarily making money by carrying on a substantial part of the activities of a person engaged in the business of selling houses, or to dispose of or liquidate the rental business. If the latter is the case, the owner obtains capital gain benefits."

The opinion of the Third Circuit in the **Curtis Company** case is set forth in Appendix "B" to this petition at page 2a.

We submit that the decision in the case at bar is in direct conflict with the **Curtis Company** case on the question of erroneous conclusions and did not apply the correct view of the law as set out in the **Curtis Company** case. The only difference in the facts is that in the **Curtis** case the taxpayer wound up the rental aspect of his property while in the case at bar the taxpayer remained in the rental business as was the intention from the beginning, and the sales were forced on the taxpayers in the case at bar.

II.

The Decision in the Case at Bar Is in Direct Conflict With the Decision of the Fifth Circuit in Nathan D. Goldberg and S. E. Wood, Jr., v. Commissioner (June 21, 1955), 223 F. (2nd) 709, on the Question of Erroneous Conclusions and Findings of Fact Induced by Erroneous View of Law.

In the **Goldberg** case, houses were constructed under F. H. A. guaranty and they were designed for rental by war workers. These houses also have restrictions on them like the case at bar and such restrictions were removed in 1945. Vacant houses were sold, as well as others, to the tenants. Sales were not advertised. The primary purpose of the corporation was renting houses. These same facts apply to the case at bar.

The Court stated:

> "Insofar * * * as the so-called 'ultimate fact' is simply the result reached by processes of legal reasoning from, or the interpretation of the legal significance of, the evidentiary facts, it is 'subject to review free of the restraining impact of the so-called "clearly erroneous" rule.' **Lehmann v. Acheson, 3 Cir., 206 F. 2d 592, 594.** As succinctly stated by Professor Moore, 'Findings of fact that are induced by an erroneous view of the law are not binding. Nor are findings that combine both fact and law, when there is error as to the law.' 5 Moore's Federal Practice, 2d Ed., Sect. 52.03 (3) * * *."

The opinion of the Fifth Circuit in the **Goldberg** case is set forth in Appendix "C" to this petition at page 14a.

We submit that the decision in the case at bar is in direct conflict with the decision of the Fifth Circuit in the **Goldberg** case on the question of an erroneous application of

the law. The evidence here as in the case at bar indicates that disposing of property, not making money from a new type of business was the primary purpose.

III.

The Decision in the Case at Bar Is in Direct Conflict With the Decision of the Eighth Circuit in Dillon v. Commissioner (June 4, 1954), 213 F. (2nd) 213, on the Question of Erroneous Conclusions and Findings of Fact Induced by Erroneous View of Law.

In the **Dillon** case, houses were constructed for rental to defense workers. This was done under F. H. A. and restrictions imposed on the sales of houses which were removed in 1945. Dillon sold 20 houses when it was not economically sound to keep them. The Question in the **Dillon** case was whether the findings were supported by the evidence or were "clearly erroneous". The Court thought that the principle applied was neither legal nor reasonable and was clearly erroneous.

The opinion of the Eighth Circuit in the **Dillon** case is set forth in Appendix "D" to this petition at page 23a.

The case at bar is similar to the **Dillon** case in that the taxpayer was not engaged in the real estate business in the sense that term usually implies.

The Question Presented Involves a Question of National Importance, Which Has Not Been But Which Should Be Settled by the Supreme Court.

The situation exists not only in the case at bar but throughout the United States of where various federal agencies force taxpayers into a position of falling prey to other federal agencies. Here the F. H. A., and O. P. A.

forced the taxpayers to sell but the taxpayer continued to remain in the same position as an "investor" and finds that he is a victim of being called a "dealer". This is not the only case where the taxpayer is called upon to pay by reason of being caught in a federal vise. There are thousands of others who are afraid to switch assets, and as a result there is being created a feudal system of land ownership.

World War II created conditions that made these tax suits, but with the conclusion of the war, the condition did not cease. What will happen in the future as to this condition will create other suits based on a misapplication of the capital gains theory.

The Court should grant certiorari and thus avoid confusion and uncertainty which will result if the Sixth Circuit's opinion in the case at bar is permitted to stand.

CONCLUSION.

Because of the conflict between the decisions in the case at bar and the **Curtis Company**, **Goldberg**, and **Dillon** cases, as well as the National importances, the writ of certiorari should issue.

Respectfully submitted,

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September [illegible], 1958.

APPENDIX.

APPENDIX A.

I. R. C. Sec. 117. **Capital Gains and Losses.**

"(a) Definitions. As used in this chapter—

"(1) **Capital Assets.** The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l), or an obligation of the United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, or real property used in the trade or business of the taxpayer;

"(j) Gains and losses from involuntary conversion and from the sale or exchange of certain property used in the trade or business.

"(1) Definition of property used in the trade or business. For the purpose of this subsection, the term 'property used in the trade or business' means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not—(A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. Such term also includes timber with respect to which subsection (k) (1) or (2) is applicable."

APPENDIX B.

Curtis Company (Formerly Curtis Engineering Company), Petitioner,

v.

Commissioner of Internal Revenue, Respondent.

Nos. 11764 and 11765.

United States Court of Appeals Third Circuit.

Argued Feb. 7, 1956.

Decided March 30, 1956.

In proceeding upon review of decision of Tax Court, the Court of Appeals, Goodrich, Circuit Judge, held, in part, that where taxpayer, normally engaged in business of buying land, and building and selling houses, built, between 1942 and 1944, 1,098 units of single and multiple housing for rental purposes, and from 1946 to 1950 disposed of units separately, and reinvested proceeds in development of rental shopping centers, and such sales were made by taxpayer's own staff, with some advertising, for cash, in "as is" condition, and taxpayer thereafter wound up rental property aspect of its business, such rental property was not held by taxpayer primarily for sale to customers in ordinary course of trade or business, and was taxable only as capital gain.

Judgment reversed and case remanded.

McLaughlin, Circuit Judge, dissented.

1. **Internal Revenue Key 1689**

Though determination by Tax Court, that property owned by taxpayer was held primarily for sale to customers in ordinary course of trade or business, sounded like fact conclusion, it would be subject to reversal upon review by Court of Appeals if conclusion was clearly erroneous, or if findings of fact were induced by erroneous view of law, 26 U. S. C. A. (I. R. C. 1939), §§ 117 (a) (1), (j) (1), 1141 (a); Fed. Rules Civ. Proc., rule 52 (a), 28 U. S. C. A.

2. **Internal Revenue Key 412**

Where taxpayer, normally engaged in business of buying land, and building and selling houses, built, between 1942 and 1944, 1,088 units of single and multiple housing for rental purposes, and from 1946 to 1950 disposed of units separately, and reinvested proceeds in development of rental shopping centers, and such sales were made by taxpayer's own staff, with some advertising, for cash, in "as is" condition, and taxpayer thereafter wound up rental property aspect of its business, such rental property was not held by taxpayer primarily for sale to customers in ordinary course of trade or business, and was taxable only as capital gain. 26 U. S. C. A. (I. R. C. 1939), § 117 (a) (1), (j) (1), 1141 (a); Fed. Rules Civ. Proc., rule 52 (a), 28 U. S. C. A.

3. **Internal Revenue Key 1689**

In proceeding upon review of determination of Tax Court, evidence sustained conclusion of Tax Court that undeveloped land, owned by taxpayer who was primarily engaged in business of buying land and building and selling houses, and who bought undeveloped land from time to time, was held primarily for sale to customers in ordinary course of trade or business, and thus sales of

undeveloped land were excluded from capital gain treatment. 26 U. S. C. A. (I. R. C. 1939), §§ 117 (a) (1), (j) (1), 1141 (a); Fed. Rules Civ. Proc., rule 52 (a), 28 U. S. C. A.

Robert Ash, Washington, D. C. (Carl F. Bauersfeld, Washington, D. C., Fred L. Rosenbloom, Thomas P. Glassmoyer, Philadelphia, Pa., on the brief), for petitioner.

Herbert Brownell, Jr., Atty. Gen., Charles B. Freeman, Washington, D. C. (H. Brian Holland, Asst. Atty. Gen., Lee A. Jackson, Harry Baum, Dept. of Justice, Washington, D. C., on the brief), for respondent.

Before Goodrich, McLaughlin and Kalodner, Circuit Judges.

Goodrich, Circuit Judge.

These appeals present the question whether the taxpayer is entitled to the benefit of capital gains provisions of the income tax statute in the business transactions described here. The Tax Court has held that the taxpayer is liable for ordinary income tax[1] and the two appeals represent the taxpayer's litigation contesting the conclusion reached for different years of its business.

[1] The sole question is one which comes under section 117 of the Internal Revenue Code of 1939, specifically (a) (1) and (j) (1) of that section. 26 U. S. C. A., § 117 (a) (1), (j) (1). What was decided by the Tax Court and what we must review here is whether specified property owned by the taxpayer was held "primarily for sale to customers in the ordinary course of his trade or business." This sounds like a fact conclusion.[2] But it is subject to

[1] Curtis Co., 1955, 23 T. C. 740.

[2] Cohn v. Commissioner, 9 Cir., 1955, 226 F. 2d 22, 24; King v. Commissioner, 5 Cir., 1951, 189 F. 2d 132, 124, certiorari denied 342 U. S. 820, 72 S. Ct. 54, 96 L. Ed. 627; Harriss v. Commissioner, 2 Cir., 1944, 143 F. 2d 279, 281.

reversal if the conclusion is clearly erroneous[3] or if the findings of fact are induced by an erroneous view of the law.[4] The point was recently stated by this Court as follows: "In disturbing a district court's findings of basic facts, this court is guided by the 'clearly erroneous' provision of Rule 52 (a). But Rule 52 (a) is not applicable where, as here, the dispute is not as to the basic facts, but as to what inference (i. e., ultimate fact) should reasonably be derived from the basic facts. * * *" Sears, Roebuck & Co. v. Johnson, 3 Cir., 1955, 219 F. 2d 590, 591. Again, to the same effect: "The District Court found as a fact that *expatriation had* taken place. With respect to that finding it must immediately be noted that it was in the nature of an ultimate finding of fact and on that score it is well settled that such a finding is but a legal inference from other facts and as such is subject to review free of the restraining impact of the so-called 'clearly erroneous' rule applicable to ordinary findings of fact by the trial court. * * *" Lehmann v. Acheson, 3 Cir., 1953, 206 F. 2d 392, 394; see also, Goldberg v. Commissioner, 5 Cir., 1955, 223 F. 2d 709, 711.

There are two chapters to the taxpayer's story. One has to do with the sale of houses; the other has to do with the sale of unimproved land.

I. Sale of Houses.

The house question will be considered first. The taxpayer during the years 1942 through 1944 built 1,098 units of housing for rental purposes. 858 units of these were single family homes; 240 were duplex apartments. Petitioner, prior to this, had bought land, divided it, built

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[3] 26 U. S. C. A. § 1141 (a); Fed. Rules Civ. Proc., rule 52 (a), 28 U. S. C. A.

[4] 5 Moore, Federal Practice, ¶ 52.03 [2], at p. 2631 (2nd ed. 1951); Goldberg v. Commissioner, 5 Cir., 1955, 223 F. 2d 709, 711.

houses thereon and sold them. This was an established division of its business and through the years ordinary income tax was paid on the profits resulting. Likewise, ordinary income tax was paid on profits derived from the rental of the houses just described.

In 1946 the restrictions on the prices at which these houses could be sold were removed.[2] Restrictions were still retained upon the price at which the property could be rented, however. The taxpayer decided to sell the houses and put its capital into the development of shopping centers, for rental purposes. It doubted whether the market value of the houses would continue to appreciate. The taxpayer thereupon made efforts to sell the houses. 851 units were sold in its tax year ending in 1947; 2 in 1948; 76 in 1949 and 45 in 1950. A gross profit of $2,829,742.81 was realized in 1947; $8,560.08 in 1948; $638,043.98 in 1949 and $377,626.31 in 1950.

The method adopted by the taxpayer was as follows: Sales were made by taxpayer's own staff. This saved the taxpayer money; its commissions were much less than if it had employed real estate brokers at the established 5 per cent commission price. Some advertising was used, more in the case of the single residences than in the case of the duplex apartments. The sales were for cash. No inspection of the properties was permitted. They were all sold in the condition in which they then were; no effort was made to improve their appearance or to make them more saleable. No additional properties of similar nature were bought by the taxpayer nor were any properties not owned by it sold in this fashion. When the rental properties were all sold the rental part of the taxpayer's business was wound up. Upon these facts, is a conclusion

[2] National Housing Agency Regulation 60-17, 10 Fed. Reg. 1272 (1945). These restrictions were imposed when priorities for building materials were obtained.

justified to the effect that these rental properties which were to be sold were held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business?

We find helpful language used by Judge Tuttle for the court in Goldberg v. Commissioner, 5 Cir., 1955, 223 F. 2d 709, 712. The court says:

> "(2) In the typical case it is clear that the property owner did not intend to engage in the business of buying and selling real estate when he acquired or developed it, but on the contrary intended only to rent it. At the time he may have been restrained from selling by wartime legislation or the terms of a government loan. But years later, his intention changes, or the government restrictions are removed, and he proceeds to sell the property. The test as to whether the capital gain provisions apply in such event is, at bottom, whether the purpose of the sales is primarily making money by carrying on a substantial part of the activities of a person engaged in the business of selling houses, or to dispose of or liquidate the rental business. If the latter is the case, the owner obtains capital gain benefits."

There is no doubt in this particular case that prior to the decision to sell these houses the properties were being held for investment purposes. The Tax Court so states and explicitly says that "up until the decisions to sell its rental houses and apartments, petitioner had [not] done anything which would disqualify these rental units for capital gains treatment under section 117 (j) upon their sale."

The court, however, did conclude that because of the manner in which the sales were made they were conducted in the ordinary course of business of selling real property. It was expressly pointed out, however, that the court

did not rely merely on the large number of sales involved but upon the various actions by the taxpayer.

It was conceded by counsel for the Commissioner at the argument that if the taxpayer had sold all these properties to one buyer at one time there would be no basis for holding that they were sold in the ordinary course of the taxpayer's business.[6] It was also conceded that had taxpayer employed a firm of brokers to sell the properties for it the sales then would not be in the ordinary course of the taxpayer's business.[7]

Is the taxpayer any worse off because it did the selling itself and by single parcels instead of job lots? We do not see how it can be fairly said so. With the concession that up to the very minute of decision to get out of the housing rental business the property was held for investment and with the undisputed fact that after the rental properties were sold the taxpayer turned its attention to other activities, we do not see that there is basis for saying that the regular course of its business, as to these houses, was real estate selling. We think it a case of one having an investment property on hand which he wants to turn into into another form of investment.[8] By the very nature of the case he had to sell the properties a piece at a time. Surely that does not make him a "dealer" in these parcels of land any more than it would make a man a dealer if he wanted to liquidate his holdings in a corporate stock for

[6] See, e. g., Chandler v. United States, 7 Cir., 1955, 226 F. 2d 403, 410; Goldberg v. Commissioner, 5 Cir., 1955, 223 F. 2d 707, 712.

[7] See, e. g., Dillon v. Commissioner, 8 Cir., 1954, 213 F. 2d 218; Smith v. Dunn, 5 Cir., 1955, 224 F. 2d 353.

[8] It is precisely this sort of thing which prompted the passage of the capital gains provisions. Capital gains were taxed at lower rates to relieve the taxpayer from "excessive tax burdens on gains resulting from a conversion of capital investments, and to remove the deterrent effect of those burdens on such conversions." Burnet v. Harmel, 1932, 287 U. S. 103, 106; 53 S. Ct. 74, 75, 77 L. Ed. 199.

which the market was weak so that he had to sell by small parcels instead of by one sale. That is the taxpayer's situation here.

[2] There is no dispute as to the evidentiary facts. The only question is whether on these facts the conclusion is supportable that petitioner went ad hoc into the ordinary course of business when it sold these rental properties. We think not.

A legislative attempt to draw a distinction between the tax on capital gain and ordinary income must necessarily produce a puzzling line of decisions for the facts are as variable as human activities. Variations of the fact situation of this case are found in a number of decisions. They indicate some disagreement not unnaturally. We think on the whole the conclusion we reach in this case is in the pattern which the majority of the Courts of Appeals have followed.[9]

II. Sales of the Unimproved Land.

Petitioner bought from time to time undeveloped land. With regard to one block of it, he has had the advantage of the capital gains provisions upon its sale. This was a piece of land which was bought for the development of a

[9] See Chandler v. United States, 7 Cir., 1955, 226 F. 2d 403; Dillon v. Commissioner, 8 Cir., 1954, 213 F. 2d 218; Greenspon v. Commissioner, 8 Cir., 1956, 229 F. 2d 947; *compare* McGah v. Commissioner, 9 Cir., 1954, 210 F. 2d 769, *with* Rollingwood Corp. v. Commissioner, 9 Cir., 1951, 190 F. 2d 263. Perhaps the Tenth Circuit would disagree with our conclusion, see Heme Co. v. Commissioner, 1954, 222 F. 2d 637. In the Fifth Circuit, *compare* Goldberg v. Commissioner, 1955, 223 F. 2d 709, *with* King v. Commissioner, 1951, 189 F. 2d 123, certiorari denied Oct. 8, 1951, 342 U. S. 829, 72 S. Ct. 54, 96 L. Ed. 627, *and* Galena Oaks Corp. v. Scofield, 1954, 218 F. 2d 217. For the Sixth Circuit, see Dougherty v. Commissioner, 1954, 216 F. 2d 110. Saltzman v. Commissioner, 3 Cir., 1955, 227 F. 2d 49, is clearly distinguishable. There the evidence indicated that the houses were never held for investment purposes. 14 T. C. M. 1955—18, C. C. H. Dec. 20,836 (M). See, generally, Reifer, Sale of Rental Housing Units: Ordinary Income or Capital Gain?, 97 Journal of Accountancy 449 (April 1954).

shopping center but the plan failed because of zoning restrictions which could not be met. The major portion of the land was sold off in two pieces at a profit. The taxpayer had the advantage of the capital gains provisions.

With regard to the other pieces the Commissioner insists that the taxpayer is not entitled to the benefit of the capital gains provisions. There were seventeen pieces held by the taxpayer during the taxable years. The taxpayer made a total of eighteen sales of undeveloped land during this period. Six of them the taxpayer conceded resulted in ordinary income.

Here, too, the evidentiary facts are not in dispute. The question is whether the taxpayer was holding this undeveloped land for sale in the ordinary course of its trade or business. The Tax Court believed the "essential fact seems to be that these properties were acquired for the purpose of re-sale whenever a satisfactory profit could be made. * * *" and "primarily for sale to its customers in the ordinary course of its business. * * *"

[3] We do not profess to know precisely what makes one a dealer in undeveloped land. There were, as those things go, quite a number of parcels and the sales were comparatively rapid. There was no such showing of a change in purpose of the taxpayer's activities to induce the sale as we had in the case of the rental properties. We cannot say under these circumstances that the Tax Court was wrong in reaching the conclusion it did.[10]

The judgment of the Tax Court will be reversed and the case remanded for further proceedings consistent with this opinion.

McLaughlin, Circuit Judge (dissenting).

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[10] See Saltzman v. Commissioner, 14 T. C. M. 1955—18, C. C. H. Dec. 20,836 (M), affirmed per curiam, 3 Cir., 1955, 227 F. 2d 49; Mauldin v. Commissioner, 10 Cir., 1952, 195 F. 2d 714.

Section 117 (j) of the Internal Revenue Code of 1939, as amended, 26 U. S. C. 117 (j), accords capital gain treatment to "property used in the trade or business" unless the property is inventory or "held * * * for sale to customers". The Supreme Court recently in construing this section stated "since this section is an exception from the normal tax * * * [it] must be narrowly applied and its exclusions interpreted broadly."[1] Our Saltzman v. Commissioner, 3 Cir., 1955, 227 F. 2d 49 is very much in point and does, I think, govern here. By any and all of the established criteria, i. e. purpose of acquisition, improvements made on the land, number of sales, advertising and selling efforts, the "busyness" test,[2] reinvestment of proceeds, related activities, this income was ordinary profit of the taxpayer's building and real estate business.

Such conclusion has the solid support of the pertinent decisional law. Cohn v. Commissioner, 9 Cir., 1955, 226 F. 2d 22; Rollingwood Corp. v. Commissioner, 9 Cir., 1951, 190 F. 2d 263; Home Co. v. Commissioner, 10 Cir., 1954, 212 F. 2d 637; King v. Commissioner, 5 Cir., 1951, 189 F. 2d 122, certiorari denied 342 U. S. 829, 72 S. Ct. 54, 96 L. Ed. 627;[3] Galena Oaks Corp. v. Scofield, 5 Cir., 1954, 218 F. 2d 217; Winnick v. Commissioner, 6 Cir., 1952, 199 F. 2d 374; Id., 21 T. C. 1029, affirmed, 6 Cir., 1955, 223 F. 2d 266; Dougherty v. Commissioner, 6 Cir., 1954, 216 F. 2d 110; involve substantially similar fact problems and clearly uphold the Tax Court. In Goldberg v. Commissioner, 5 Cir., 1955, 223 F. 2d 709, 713, "[t]here was absolutely no evidence of any promotional activity * * *"; there was no advertising; no salesmen; no commissions paid; though price ceilings had been removed, the houses were sold to tenants at the

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[1] Corn Products Refining Co. v. Commissioner, 1955, 350 U. S. 46, 52, 76 S. Ct. 20, 24.

[2] Snell v. Commissioner, 5 Cir., 1938, 97 F. 2d 891.

[3] For later year on same facts see Jackson v. King, 5 Cir., 1955, 223 F. 2d 714, reversing jury verdict for taxpayer.

F. H. A. prices; neither the taxpayer nor any of the transferees there had ever before or since been in the business of building and holding houses for sale. In Dillon v. Commissioner, 8 Cir., 1954, 213 F. 2d 218, the taxpayer was not in the real estate business and all the sales promotional activity was carried on by an outside real estate company. The same is true of Smith v. Dunn, 1955, 224 F. 2d 353, Fifth Circuit (one judge dissenting in part). McGah v. Commissioner, 9 Cir., 1954, 240 F. 2d 769 involved a forced partial liquidation, at the behest of a creditor bank. Chandler v. United States, 7 Cir., 1955, 226 F. 2d 403 involved a unique fact situation[4] and the court gave great weight to the fact that there was no reinvestment of the proceeds in real estate as we have in the present situation. Greenspon v. Commissioner, 8 Cir., 1956, 229 F. 2d 947, involved sales by liquidating trustees of a pipe business. It is at most only obliquely related to the facts before us; further, there was no extensive advertising or sales promotion.

The circumstance that these properties were not readily salable as investment real estate, reflects back on the purpose for which taxpayer built them. An apartment house is typical investment housing. It is salable as such and capital gain results. But suppose it is divided into 1,000 cooperative apartments, should not the "sale to customers" exclusion deny the favored treatment?

The analogy to a trader in securities is inapposite. Trading in securities, for one's own account, no matter how extensive, is not a business for tax purposes. Real estate operations, however, are taxable as a business. Higgins v. Commissioner, 1941, 312 U. S. 212, 61 S. Ct. 475, 85 L. Ed. 783. This taxpayer's regular business is buying land, subdividing, building, and selling real estate to consumers or

[4] There a Chicago liquidating trust of some three million acres of Texas land after forty years was still liquidating. It was not the conventional builder and realtor, as is the instant taxpayer.

investors. If analogy to the securities field is to be used it is the "underwriter" or "dealer" operation which is comparable to the taxpayer. The "dealer" or "underwriter" may have an investment account and thereby obtain capital gains, but he must conform closely to Section 117 (n) and the regulations thereunder. Even after designation within thirty days of acquisition as an investment, if the security is thereafter ever held for sale to the firm's customers the favored treatment under Section 117 is lost. A "dealer" cannot buy or underwrite a large block of securities, and, after holding more than six months, sell them piecemeal to his customers and still qualify under Section 117.

In Section 1237 of the Internal Revenue Code of 1954, Congress sharply outlined the sale of realty area. Taxpayer's facts patently would not qualify for favored treatment under that section. And "* * * 'subsequent legislation may be considered to assist in the interpretation of prior legislation upon the same subject.' * * *" Great Northern Railway Co. v. United States, 1942, 315 U. S. 262, 277, 62 S. Ct. 529, 535, 86 L. Ed. 836.

The basis of the majority thesis is that property once "used in a trade or business" retains that character regardless of whether it is subsequently inventoried or held for sale to customers. Section 117 has not been and cannot be so construed but is the sound source of the well established principle that manner and purpose of holding property may change or be twofold. Richards v. Commissioner, 9 Cir., 1936, 81 F. 2d 369, 166 A. L. R. 249; and Cohn v. Commissioner, supra; Rollingwood Corp. v. Commissioner, supra; Home Co. v. Commissioner, supra; King v. Commissioner, supra; Galena Oaks Corp. v. Scofield, supra; Winnick v. Commissioner, supra; Dougherty v. Commissioner, supra.

In selling the houses taxpayer was engaged in business. It should be so taxed. I would therefore affirm the Tax Court on this point also.

APPENDIX C.

Nathan D. Goldberg and S. E. Wood, Jr.

v.

Commissioner of Internal Revenue.

No. 15317.

United States Court of Appeals
Fifth Circuit.

June 21, 1955.

Proceeding on petition by taxpayers for review of adverse decision of United States Tax Court, 22 T. C. 533. The Court of Appeals, Tuttle, Circuit Judge, held that where corporation erected large number of housing units for rental purposes and subsequently, due to poor return from rental business, began selling such units to their occupants, houses sold were not held primarily for sale to customers in ordinary course of trade or business, and profit realized from such sales was not taxable as ordinary income but as capital gain.

Reversed and remanded.

1. **Internal Revenue Key 1682**

Findings of fact of tax court that are induced by erroneous view of law are not binding, nor are findings that combine both law and fact, when there is error as to law.

2. **Internal Revenue Key 412**

Test as to whether capital gain provisions of internal revenue code apply in determining whether sale of property by persons who originally constructed such housing for rental purposes, is whether purpose of sale was primarily making money by carrying on substantial part of

activities of person engaged in business of selling houses, or to dispose of or liquidate rental business, and if latter is case, owner obtains capital gain benefits.

3. **Internal Revenue Key 412**

Where corporation erected large number of housing units for rental purposes and subsequently, due to poor return from rental business, began selling such units to their occupants, houses sold were not held primarily for sale to customers in ordinary course of trade or business, and profit realized from such sales was not taxable as ordinary income but as capital gain. 26 U. S. C.A., § 117 (j) (1) (B).

Tom B. Rhodes, Geo. S. Atkinson, Dallas, Tex., for petitioners.

S. Dee Hanson, Ellis N. Slack, Hilbert P. Zarky, Alonzo W. Watson, Jr., Sp. Assts. to Atty. Gen., H. Brian Holland, Asst. Atty. Gen., Daniel A. Taylor, Chief Counsel, and Charles E. Lowery, Sp. Atty., Internal Revenue Service, Washington, D. C., for respondent.

Before Hutcheson, Chief Judge, and Tuttle and Jones, Circuit Judges.

Tuttle, Circuit Judge.

The sole question presented in these petitions for review is the propriety of the Tax Court's finding of fact that 90 houses sold by Pinecrest Housing, Inc., in 1946, were then held primarily for sale to customers in the ordinary course of trade or business. The Tax Court, in an opinion reported at 22 T. C. 533, held the petitioners liable as transferees, for a corporation income tax deficiency for 1946, redetermined against Pinecrest on the ground that the $58,675.41 profit realized on the sales of the houses, and reported by it as a capital gain, was taxable as ordinary income. Since petitioners admit they are transferees of

the assets of Pinecrest, the decision of the Tax Court must be affirmed unless it was clearly erroneous in its finding that the houses were in 1946 held primarily for sale to customers in the ordinary course of trade or business. 26 U. S. C., § 117 (j) (1) (B) (1946 Ed.).

The following statement of facts, being in substance taken from the brief of the respondent, fairly presents the evidence relied on as supporting the Tax Court's decision:

Pinecrest was incorporated under the laws of Texas in 1943, "to erect, construct, or repair any building or improvements, and to purchase, sell, rent, subdivide, and improve real property in towns, cities, villages and their subdivisions * * *." The 2,000 shares of $10 par value stock were owned as follows: S. E. Wood, Jr., and James B. Cheek, 667 shares each; Marion F. Fooshee, 666 shares. In 1943 the corporation had 111 housing units constructed in Marshall, Texas, these being two- and three-bedroom houses. At that time there was an acute need of housing in the area because of the influx of defense workers. The project was financed by an insurance company, upon the Federal Housing Administration guaranty to the extent of 90 per cent of the project's appraised value. The guaranty was conditioned on design of the houses for residential rental by war workers, and Pinecrest indicated in its application to the F. H. A. that they would be used for rental. Under the F. H. A. regulations, Pinecrest could sell the houses at a ceiling price fixed by F. H. A. to war workers who had occupied the premises four months and who agreed in writing to continue occupancy for a specified period after purchase. Effective September 10, 1945, the restrictions on sales were revoked as to housing then or thereafter vacant, provided the vacancy had not been created by eviction and that a maximum authorized sales price had been established for the housing to be sold.

In April 1944, the corporation, having difficulty meeting its mortgage payments because of insufficient rental in-

come, shareholders Cheek and Eooshee sold their stock to petitioners so as to make each the owner of 50 per cent of the stock. Pinecrest was also granted a one-year delay in making payments on the mortgage and a reduction of interest thereon. By the end of 1944, rental income increased and Pinecrest resumed full current payments on the mortgage. It reported operating losses on rentals in each of the four years of its existence, 1943 and 1946, although by the end of 1945 the housing units were almost fully occupied. However, profits were realized from the sale of houses in each of these years; in 1943, $134.50 from the sale of two houses; in 1944, $698.83 from the sale of two houses; in 1945, $7,642.16 from the sale of 17 houses and a vacant lot; and in 1946, the year in question, $58,675.41 from the sale of 90 houses. Most of the 1946 sales were to tenants, many of whom were war veterans. Property sales were handled by petitioner Goldberg, whose office received $100 a month from 1944 to 1946 for keeping Pinecrest's rental and sales records. Sales of the houses were not advertised, but their availability for sale was made known by word of mouth; no "for sale" signs were put up; no salesmen were hired; and no commissions were paid on the sales. In 1946 there was a heavy demand for housing in the area. The corporation was dissolved in December, 1946, and petitioners divided all the corporation's assets equally. Petitioner Wood, president of Pinecrest, was an automobile dealer from 1919 through 1949, was not in the business of buying and selling real estate, and did not have a real estate dealers' license, though he occasionally sold a parcel of real estate. Petitioner Goldberg, vice president of Pinecrest, was a real estate agent with 26 years' experience.[1] Before 1944 his principal ac-

[1] The Tax Court found that Goldberg was a "dealer," but the only evidence in the record showed that he "was engaged in the general real estate business of handling sales, lease rentals and trades; that property management or rentals for other people occupied most of his time." There is no evidence that he bought and sold property on his own account as a business.

tivity was managing properties for others, but he occasionally sold properties for others on commission.

On these facts, the Tax Court found that although petitioners went into business for the purpose of building houses for rental, by the beginning of 1946 the nature of the corporation's business had been changed to selling houses; therefore, that the profit realized from sales in 1946 was taxable as ordinary income and not as capital gain.

[1] First, as to the scope of the review which we may make of the Tax Court's finding that the houses were held during the taxable year for sale to customers in trade or business, we reaffirm all that we said on the subject in our recent case of Galena Oaks Corp. v. Scofield, 5 Cir., 218 F. 2d 217, 219. As Judge Rives expressed the principle applicable to the decision of the present case, as we conceive it:

> "Insofar * * * as the so-called 'ultimate fact' is simply the result reached by processes of legal reasoning from, or the interpretation of the legal significance of, the evidentiary facts, it is 'subject to review free of the restraining impact of the so-called "clearly erroneous" rule.' Lehmann v. Acheson, 3 Cir., 206 F. 2d 592, 594. As succinctly stated by Professor Moore, 'Findings of fact that are induced by an erroneous view of the law are not binding. Nor are findings that combine both fact and law, when there is error as to the law.' 5 Moore's Federal Practice, 2d Ed., Sec. 52.03 (3) * * *."

We are convinced that the finding of the Tax Court was the result of an erroneous view of the law, and proceed now to state our view of the substantive law involved.

Like other courts, we have had frequent occasion to consider this matter. Dunlap v. Oldham Lumber Co., 5 Cir., 178 F. 2d 781; Fahs v. Crawford, 5 Cir., 161 F. 2d 315; Lobello v. Dunlap, 5 Cir., 210 F. 2d 465; and Galena Oaks

Corp. v. Scofield, 5 Cir., 218 F. 2d 217, are several of the leading cases in this circuit. Since the cases are so numerous, and since practically every judicial discussion involves the particular combination of facts present in the case, it is difficult to review them in brief. But the cases follow a consistent pattern and line of reasoning; and although the courts are fond of saying that each case depends on its particular facts, we may set out some objective principles which they uniformly follow.

[2] In the typical case it is clear that the property owner did not intend to engage in the business of buying and selling real estate when he acquired or developed it, but on the contrary intended only to rent it. At the time he may have been restrained from selling by wartime legislation or the terms of a government loan. But years later, his intention changes or the government restrictions are removed, and he proceeds to sell the property. The test as to whether the capital gain provisions apply in such event is, at bottom, whether the purpose of the sales is primarily making money by carrying on a substantial part of the activities of a person engaged in the business of selling houses, or to dispose of or liquidate the rental business. If the latter is the case, the owner obtains capital gain benefits.

A significant matter in determining whether the purpose is liquidation of a business is, of course, whether, considering the objective evidence, the owner ever intended to operate a rental business in the first place. If the property was originally acquired for rental purposes, it may nevertheless later be held for ordinary business sale to customers; and the converse may also be true. But the original purpose is important, for to counterbalance it there must be significant objective evidence of a change in that purpose.

The frequency and continuity of sales is also important. If a rental corporation's assets are sold in a single trans-

action to a single purchaser, it could not be reasonably contended that there was a sale to a customer in the regular course of business. But more often the owner sells his rental properties piecemeal to different individuals. How frequent the sales are depends on many circumstances: the extent to which the seller turns his talents to the promotion and solicitation of sales, the number of units in the rental project, and the state of the market. Only the first of these circumstances has any rational connection with the question whether the owner has changed his business to selling, or is simply liquidating his business. Thus the frequency and continuity of sales factor is significant only so far as it reasonably justifies the conclusion that the owner somehow promoted the sales. The courts do not deny capital gain benefits simply because a large number of sales are made in a short period; for if the owner has a large number of houses on a seller's market, it is quite possible that he may sell them continuously without any sales promotion or solicitation.

It seems that appellate courts have quite generally upheld the finding by the trier of fact that the owner was a dealer, where the evidence showed that he himself devoted his energies and talents to substantial promotional, advertising, or sales techniques ordinarily associated with real estate dealers. Furthermore, if the owner was contemporaneously, or soon before or after, buying or selling other properties on his own account as a dealer, appellate courts have found that this evidence supported factual findings resulting in the denial of capital gain benefits with respect to the rental properties in question.

Now, let us apply these principles to the facts of the present case. The Tax Court found as a fact, and we agree, that petitioners bought the property for rental as residential property. Later they decided to sell it in individual sales. That fact points to a liquidation of capital with as much persuasiveness as to sale as a money-making

activity. The sales were frequent and continuous; but since the circumstances were favorable to selling to individuals and the project was a large one, this is entirely consistent with liquidation of it as an investment. Indeed, the evidence that is in the record indicates that disposing of the property, not making money from a new type of business, was the primary purpose. Petitioners introduced uncontradicted evidence that Pinecrest sold the houses at established F. H. A. prices, although ceiling prices had been lifted and the houses could have been sold for considerably more. There was absolutely no evidence of any promotional activity or that petitioners used the proceeds to buy and sell other houses. The fact that the rental business had been unprofitable, to which the Tax Court attached such significance, is fully as consistent with a decision to liquidate the property opportunely, as to turn it into another more profitable type of business.

[3] In short, the only evidence that the corporation was engaged in the business of selling real estate was the frequency and continuity of sales, and this for a comparatively short time. Under the circumstances, the fact was equivocal, and that fact alone is not sufficient to support a finding of the ultimate fact that Pinecrest was engaged in selling houses as a business. We conclude that the Tax Court's finding was based upon an erroneous application of the law. Lobello v. Dunlap, 5 Cir., 210 F. 2d 465; Dunlap v. Oldham Lumber Co., 5 Cir., 178 F. 2d 781; United States v. Robinson, 5 Cir., 129 F. 2d 297; Victory Housing No. 2 v. Commissioner, 10 Cir., 205 F. 2d 371.

The Tax Court relied, and respondent relies, principally on the case of King v. Commissioner, 5 Cir., 189 F. 2d 122, certiorari denied 342 U. S. 829, 72 S. Ct. 54, 96 L. Ed. 627; Rollingwood Corp. v. Commissioner, 9 Cir., 190 F. 2d 263; Home Co. v. Commissioner, 10 Cir., 212 F. 2d 637; and Winnick v. Commissioner, 21 T. C. 1029, affirmed 6 Cir., 223 F. 2d 266. But all of these cases involved some further cir-

cumstance indicating the property was held for sale to customers as a business. In King [189 F. 2d 123], the evidence showed that the taxpayer made "earnest and strenuous efforts to so sell" the houses. In Rollingwood [190 F. 2d 264], Bohannon, the sole stockholder of the corporation during the taxable year, had prior to that time engaged in "the business of subdividing and selling real property". In Home Company, there was an active sales campaign and extensive advertising. In Winnick, the taxpayer was in the business of building and selling houses (other than the ones in question) during the taxable year, and had been for a period of seven years. These cases are distinguishable, for here there was no evidence at all of any activities that would indicate the conduct of business of selling houses as distinguished from liquidating a rental business as rapidly as possible consistent with a desire to realize the benefits of individual rather than bulk sales. Moreover, it is to be remembered that neither the corporation nor petitioner had ever engaged in the business of selling real estate held by himself. Goldberg's occupation of managing the properties of others and making sales for others on commission was quite obviously not the same as dealing in real estate on his own account.

The judgment is reversed and the case remanded for entry of judgment in favor of petitioners.

APPENDIX D.

Dillon

v.

Commissioner of Internal Revenue.

No. 14964.

United States Court of Appeals
Eighth Circuit.

June 4, 1954.

Petition by taxpayer to review decision of Tax Court of United States. The Court of Appeals, Thomas, Circuit Judge, held that where contractor organized corporation, that signed mortgages, in 1943 to carry out construction of houses, which when completed were deeded to contractor and rented to defense workers in cooperation with federal housing administration, and contractor, who was not in the real estate business in 1946 and did not hold a real estate license, sold 20 houses in 1946 through corporation that was engaged in the real estate business, gain realized by contractor was taxable as a capital gain and not as ordinary income.

Decision of Tax Court reversed.

Internal Revenue Key 412

Where contractor organized corporation that signed mortgages in 1943 to carry out construction of houses, which when completed were deeded to contractor and rented to defense workers, and contractor, who was not in the real estate business in 1946, sold 20 houses in 1946 through corporation that was engaged in the real estate business, gain realized by contractor was taxable as a

capital gain and not as ordinary income. National Housing Act, § 601 et seq., 42 U. S. C. A., § 1736 et seq.; 26 U. S. C. A., §§ 22 (a), 117 (a), and (1), (j) and (l), 1141 and (a).

Robert Ash, Washington, D. C. (Carl F. Bauersfeld, Washington, D. C., and Marvin G. Schmidt, Omaha, Neb., were with him on the brief), for petitioner.

Louise Foster, Sp. Asst. to the Atty. Gen. (H. Brian Holland, Asst. Atty. Gen., and Ellis N. Slack and Dudley J. Godfrey, Jr., Sp. Assts. to the Atty. Gen., were on the brief), for respondent.

Before Gardner, Chief Judge, and Woodrough and Thomas, Circuit Judges.

Thomas, Circuit Judge.

This case comes to this court on the petition of a taxpayer to review a decision of the Tax Court of the United States. The questions presented are (1) whether the gain realized from the sale of 20 housing units by petitioner during the calendar year 1946 was taxable as a capital gain under § 117 (a) and (j) of the Internal Revenue Code, 26 U. S. C. A., or as ordinary income under § 22 (a); and (2) is the decision of the Tax Court in error in failing to allow the petitioner credit for a portion of the tax paid subsequent to the issuance of a notice of deficiency?

Jurisdiction is conferred on this court by § 1141 (a) of the Internal Revenue Code as amended May 24, 1949, c. 139, § 128, 63 Stat. 107.

The evidentiary facts are not in dispute. From 1937 to 1941, inclusive, Dillon, the petitioner, was engaged in building houses for sale in Des Moines, Iowa. After Government regulations prevented private building in Des Moines in 1943, Dillon went to Omaha, Nebraska, and discussed the housing situation there with Federal Housing

Administration officials, referred to in the record as F. H. A. An acute housing shortage existed in Omaha because several defense plants were located in that area and because many defense workers had moved there. The F. H. A. officials encouraged Dillon to move to Omaha and build rental housing for such workers under Title VI of the National Housing Act, 42 U. S. C. A., 1726 et seq. Dillon went to Omaha, and, at the suggestion of the F. H. A. officials organized a corporation for the purpose of carrying out the construction of houses.

In all of his applications for priorities for building material Dillon agreed to hold the houses for rent to war workers at a fixed monthly rental and not to dispose of them except as authorized by the National Housing Agency. Orders were issued permitting the sale of a limited number of houses to war workers, and after August 1, 1943, the owner constructing houses could sell one-third of them.

The corporation which Dillon organized held title to the houses and the land on which they were constructed. When the 20 houses in issue were completed in 1944 and 1945 they were deeded to Dillon. He testified that they were deeded to him "Because actually the corporation was just a dummy to sign the mortgages and I own them personally, in fact, so they deeded them back after the houses were completed."

Upon completion of the houses they were rented to war workers on oral month-to-month tenancies under rentals approved by the F. H. A.

On October 15, 1945, all restrictions on the sale and rental of defense housing were removed by the National Housing Agency and the War Production Board. Sometime thereafter Dillon decided to sell the 20 houses because he thought it was no longer economically sound to keep them.

The 20 houses were all sold in 1946, most of them to veterans. The sales were handled by the Western Securities Company for which it received a commission of about 5 per cent of the sale price. Dillon did not hold a real estate dealer's license in 1946. He held no other rental property during the years 1942 to 1945 inclusive other than the houses he constructed under the defense housing program.

The Tax Court found "* * * that the 20 houses in question were held primarily for sale to customers in the ordinary course of business in the taxable year and net profits derived from the sale thereof during said year are taxable as ordinary income."

Section 22 (a) of the Internal Revenue Code reads in essential part: "'Gross income' includes gains, profits, and income derived from * * * sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property * * *."

Section 117 (a) (1) provides: "The term 'capital assets' * * * does not include * * * property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business; * * *."

And § 117 (j) (1) reads in part: "* * * the term 'property used in the trade or business' means * * * not * * * (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

The question for determination is, therefore, whether the findings of the Tax Court are supported by the evidence or are "clearly erroneous." 26 U. S. C. A., § 1141; Rule 52 of the Federal Rules of Civil Procedure, 28 U. S. C. A.

In its opinion the court said: "We must determine the purpose for which the property is held during the taxable years in question * * *. From the record it is apparent the houses were held for rental purposes to October 15, 1945,

the date when the restrictions on the sale of defense housing were removed. The record also shows that after that the houses were held for sale."

What was the business of the taxpayer after October 15, 1945? It was no longer the building of houses for rent. Was it the liquidation of his former business or was it the real estate business?

In the recent decision of the Tenth Circuit Court of Appeals in Home Co., Inc., v. Commissioner of Internal Revenue, 10 Cir., 212 F. 2d 637, the court say:

> "One may, of course, liquidate a capital asset. To do so it is necessary to sell. The sale may be conducted in the most advantageous manner to the seller and he will not lose the benefits of the capital gain provision of the statute, unless he enters the real estate business and carries on the sale in the manner in which such a business is ordinarily conducted. In that event, the liquidation constitutes a business and a sale in the ordinary course of such a business and the preferred tax status is lost."

The petitioner was not engaged in the real estate business in the sense that term usually implies. He did not have a license to act as a real estate agent. When he decided to sell the 20 houses in issue he advertised them in a local paper. The Tax Court found that "Sales negotiations were handled by the Western Securities Company for which it received a commission of about 5 per cent of the sales price."

The Tax Court bases its determination upon the ground that "We must determine the purpose for which the property is held during the taxable year [1946] in question," and that after October 15, 1945, "the 20 houses in question were held primarily for sale to customers in the ordinary

course of business in the taxable year and net profits are taxable as ordinary income." The 20 houses were sold during the period from January 1, 1946, to August 8, 1946. The Court arrives at its conclusion on this point by a consideration of the business done in the taxable year 1946, and attaches no significance to the resolution of the taxpayer to liquidate his holdings in the houses in the fall of 1945. The Court cites one of its own opinions only to support its theory. Strictly applying this rule had the taxpayer decided to liquidate his holdings in December, 1945, and failed to complete the liquidation before January, 1946, the result would have been the same. Neither a statute nor the decision of any court is cited to support the theory of the Tax Court. We think the principle applied is neither legal nor reasonable, but that it is clearly erroneous. Under the evidence here the petitioner was not in the real estate business in Omaha in 1946. He was liquidating his ownership of 20 houses through a corporation engaged in the real estate business. There is no conflict in the evidence on this decisive point.

The petitioner contends further that the Tax Court erred in failing to allow credit for a portion of the tax paid subsequent to the issuance of the notice of deficiency. The amount of the alleged payment is not stated in the record nor in the brief. Since we are reversing the decision of the Tax Court, no doubt the Government will settle this matter fairly with the taxpayer.

The decision of the Tax Court is reversed.